COUNCILMEMBER DONNA FRYE
City of San Diego
Sixth District

MEMORANDUM

DATE: February 16, 2007

TO: Mayor Jerry Sanders
Michael Aguirre, City Attorney

FROM: Councilmember Donna Frye Donna Frye

SUBJECT: Bank of America

A recent article in the *New York Times* (attached) has raised concerns regarding Bank of America's bidding practices in the municipal bond market. The article states that the Justice Department has been investigating these practices, particularly examining if there was any collusion among financial institutions in bidding to handle bond revenue during the interim period between when the money is raised and when it is spent on municipal projects.

Since the city recently entered into an agreement with Bank of America to refund the ballpark bonds, this information greatly concerns me. Please provide me with a report regarding if this situation affects the city's refunding of the ballpark bonds or any other municipal transactions between the city and Bank of America.

cc: Honorable City Councilmembers
Deputy City Attorney, Mark Blake, DPWG
Andrea Tevlin, Independent Budget Analyst
City Auditor and Comptroller

DF/ks

The New York Times
nytimes.com

February 10, 2007

U.S. Inquiry on Bonds at Big Bank

By VIKAS BAJAJ

Bank of America said yesterday that it was cooperating with a Justice Department investigation into bidding practices in the municipal bond business in exchange for leniency.

The agreement with the bank may be a significant breakthrough for government investigators who have been looking at how the proceeds of bonds issued by cities, school districts and other municipal authorities are invested between the time the money is raised and when it is spent on projects like new water systems and school gymnasiums.

Investigators are examining whether there was collusion among some financial institutions in bidding to handle the bond revenue during those interim periods.

Last November, the Justice Department issued subpoenas and raided the offices of several firms that served as go-betweens for municipalities and large financial institutions.

The investigation is the biggest in municipal finance since the 1990s, when the Securities and Exchange Commission accused some Wall Street firms of "yield burning" — or profiting by overcharging state and local government agencies in debt refinancings. The current investigation is unusual because it appears to involve possible criminal charges.

Bank of America said the Justice Department had agreed not to bring criminal charges against the bank because it was the first institution to volunteer information before the subpoenas were issued. Furthermore, the agreement limits the civil penalties that prosecutors can pursue against the bank to actual damages, rather than the treble damages it can pursue against others.

The deal, which the bank said would not be available to other financial institutions, is contingent on continued cooperation by Bank of America.

"If a company has participated in industrywide practices, its cooperation can prove invaluable," said Kathleen F. Brickey, a law professor at Washington University in St. Louis who specializes in white-collar crime. as prosecutors investigate other companies. "This will be unwelcome news for others" in the industry.

In a separate settlement with the Internal Revenue Service, Bank of America said yesterday that it would pay $14.7 million to the federal government for its role in the use of contracts that provided guaranteed investment returns on proceeds from bond pools issued by multiple municipalities. The I.R.S. has been examining whether such pools are being used to generate profits from tax-free municipal bonds.

"They are related only in that the two are happening at the same time and involve the municipal arena," said Shirley Norton, a Bank of America spokeswoman.

A spokeswoman for the Justice Department confirmed that it had reached an agreement with Bank of America but would not answer questions about the deal. A spokesman for the I.R.S. declined to comment.

Municipal bonds are a big business for Wall Street — about $385 billion of bonds were issued last year, according to the Securities Industry and Financial Markets Association. The bonds provide a steady source of fees and are a relatively safe, and tax-free, investment.

In recent years, several government agencies, including the Securities and Exchange Commission, have focused on how the proceeds of the bonds are handled in the months or years before they are spent. Because the money is tax-free, municipalities cannot generate a higher return on the money by investing it than what it costs to raise the money. If they do earn more, the balance is due to the United States Treasury.

To get around those limits, consultants to municipalities and major financial institutions like Bank of America have used guaranteed investment contracts that limit the return cities and other agencies can earn from their bond proceeds.

Investigators are looking into whether some financial institutions have colluded when bidding for those contracts, which are structured in a way that appeared to satisfy the I.R.S. rules but in reality provide excessive fees or returns to banks and advisers involved in the transactions.

“Municipal bond proceeds are supposed to be spent for tangible purposes, not to earn interest in arbitrage,” said Charles Anderson, a retired I.R.S. field inspector who now has a private consulting practice. “You want a transparent and above- board process of people getting investment contracts.”

In November, Bloomberg News reported that federal agents raided and seized documents from the offices of three brokers that specialized in municipal finance and Justice Department lawyers subpoenaed documents from two insurance companies and General Electric.

Shares of Bank of America slipped 33 cents, to $52.99.